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IN THE
Supreme Court of the United States

OCTOBER TERM, 1948.

No. 356

THE CENTURY INDEMNITY COMPANY,

Petitioner,

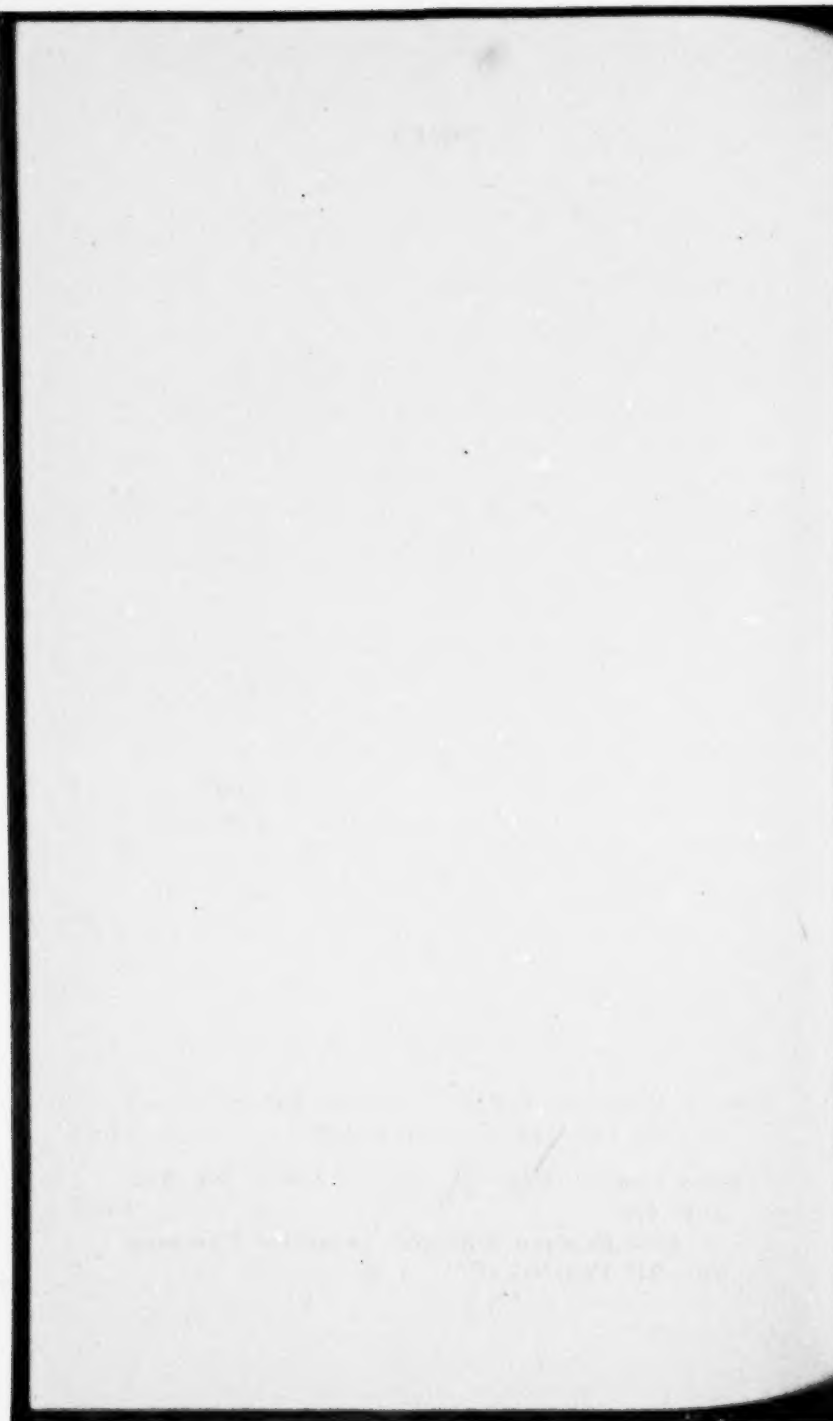
—against—

RICHARD L. ROSENBAUM, Trustee in Bankruptcy for
Ultimate Corporation, Bankrupt, and GRAYS
FERRY BRICK COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
AND BRIEF IN SUPPORT THEREOF.

SAMUEL GOTTESMAN,
Attorney for Petitioner,
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New York City.



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—against—

RICHARD L. ROSENBAUM, Trustee in Bankruptcy for
Ultimate Corporation, Bankrupt, and GRAYS
FERRY BRICK COMPANY,

Respondents.

**Petition for Writ of Certiorari to the United States
Court of Appeals for the Second Circuit.**

Samuel Gottesman, on behalf of The Century Indemnity Company, prays that a writ of certiorari issue to review the judgment entered in this case on the 7th day of July, 1948, by the United States Circuit Court of Appeals for the Second Circuit reversing an order entered in the United States District Court for the Southern District of New York in favor of the petitioner, directing the trustee in bankruptcy of Ultimate Corporation to turn over to petitioner the sum of \$3762.22 out of a fund of \$4119.23, in the hands of the trustee, and representing the final payment made by the United States of America under a contract with the bankrupt for certain construction work at Scituate, Mass.

A certified transcript of the record in the case, including the proceedings in the Circuit Court of

Appeals, is furnishd herewith in accordance with the rules of this Court.

An application for rehearing was timely made in the Circuit Court of Appeals and denied by order of that Court filed on July 24th, 1948.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals appears at R., pp. 72-76.

The opinions of the Referee in Bankruptcy, whose orders were confirmed by the District Court without opinion (but which order of the District Court was reversed by the Circuit Court) appear at R., pp. 63-68.

JURISDICTION.

The judgment of the Circuit Court of Appeals was filed on July 7th, 1948 (R., p. 7~~8~~). The order denying the petition for rehearing was filed on July 24th, 1948 (R., p. 90).

Jurisdiction of the District Court was based on the fact that the proceeding in which petitioner's original application was made was then pending in said Court (Bankruptcy Part). The two orders of the Referee above referred to were confirmed by the District Court. From the said order of the District Court, the respondents appealed to the Circuit Court of Appeals for the Second Circuit.

This Court, by virtue of Subdivision (a) of Section 240 as amended of the Judicial Code (28 U. S. C. A. Section 347) has power and authority, acting upon this petition to require certification, to it, by certiorari, of the cause before the Circuit Court of Appeals, in-

cluding its judgment for purposes of full review and determination.

STATUTE INVOLVED.

The bond executed by petitioner and under which its rights in this action derive, is known as a Miller Act bond and was required to be filed by Ultimate Corporation, the bankrupt, by 40 U. S. C. A. Section 270(a), which provides, insofar as here material, as follows:

“(a) Before any contract, exceeding \$2,000.00 in amount, for the construction, labor, or repair of any public building or public work of the United States, is awarded to any person, such person shall furnish to the United States, the following bonds, which shall become binding upon the award of the contract to such person, who is hereinafter designated as ‘contractor’.

* * * *

(2) A payment bond with a surety or sureties satisfactory to such officer for the protection of all persons supplying labor and material in the prosecution of the work provided for in said contract for the use of which such person * * *.”

QUESTIONS PRESENTED.

The Circuit Court of Appeals erred:

(1) In failing to decide the rights of petitioner, surety on a bond given pursuant to a federal statute, solely on the basis of the rule of priority enunciated by the federal courts in favor of sureties on this type of bond.

(2) In failing to accord to petitioner the paramount right to the fund in question, accorded to sureties on this type of bond by the decisions of the Supreme Court and of other Circuit Courts of Appeals.

(3) Even assuming that New York State law applies—in failing to decide petitioner's rights on the basis of New York State decisions on similar types of bonds in connection with state construction contracts, in which the New York State Courts have laid down the identical rule of priority as have the federal cases.

(4) In basing its reversal solely on New York State decisions in no way involving the rights of sureties under Miller Act bonds or rights of sureties under similar bonds given in connection with state construction contracts.

(5) In holding that the question of whether the equitable lien possessed by the surety on the fund in question was paramount to the lien of Grays Ferry Brick Co. or the lien of the trustee in bankruptcy under Section 70(c) of the Bankruptcy Act, must be determined by New York law.

(6) In holding that the trustee in bankruptcy and Grays acquired a lien on a fund which was never the property of the bankrupt.

(7) In holding that if any equitable lien arose in favor of the surety that it would be subordinate to the rights of Grays (the judgment creditor) and the trustee in bankruptcy.

(8) In suggesting that it was questionable whether

any lien that petitioner might have would extend to any amounts other than the reserved percentage on the federal contract in question.

STATEMENT OF THE CASE.

The facts were stipulated and are contained in the Record at pages 36-47. In simple outline, however, they are as follows:

The trustee in bankruptcy is in possession of a fund which represents the final payment made by the government under a contract with the bankrupt for the construction of a building at Scituate, Mass. The existence, identity and tracing of the fund is conceded. No rights of bona fide purchasers for value and without notice are involved. The fund is claimed by petitioner by virtue of its subrogation to the rights of labor and material creditors on the construction contract in question, to whom petitioner made payment under its payment bond and by virtue also of assignments from those creditors. Grays Ferry Brick Co. (the judgment creditor) claims a lien thereon by virtue of a Third Party Order in Supplementary proceedings served by it on the bank in which the fund was deposited before it came into the hands of the trustee in bankruptcy. Grays' judgment was not for any labor or material furnished to the bankrupt in the prosecution of its contract with the government and its Third Party order was served on the bank on the very day on which the bankrupt executed an assignment for the benefit of creditors and one week before an involuntary petition in bankruptcy was filed against it.

The trustee in bankruptcy claims the fund pursuant to Section 70(c) of the Bankruptcy Act which confers

upon a trustee the rights of a creditor holding a lien, or judgment creditor holding an execution returned unsatisfied, as of the date of bankruptcy.

On petitioner's application, the Referee in Bankruptcy held (R., pp. 63-68) that persons supplying labor and materials to a contractor in the prosecution of the work provided for in a government contract, have an original and continuing equitable priority in the moneys payable upon performance of that contract and that the surety on the payment bond of the contractor, upon paying those persons, is subrogated to that right; that the surety's right of subrogation to the superior equities of such labor and material creditors dates back to the execution of its bond; that the weight of authority of the federal decisions on this subject has been followed by the Courts of New York as respects both the surety on a completion bond and the surety on a material and labor payment bond on state construction contracts; that the fund in question was created and in existence, capable of identification before any lien was acquired by the trustee or the judgment creditor, neither of whom is in the position of a bona fide purchaser for value without notice; that the trustee in bankruptcy acquired no rights against the surety; that the only right of the bankrupt to the fund was in any surplus remaining after full payment had been made to labor and material creditors, and that the trustee acquired no greater interest therein; that the surety's right of subrogation to laborers and materialmen in the fund is paramount to the right of the contractor's trustee in bankruptcy and paramount also to the judgment creditor's lien, which if valid, is superior only to the trustee's; that the contention that local law gives a lien creditor precedence over

the subrogated surety has no application to contracts which originated under the Miller Act, and that the contention of the trustee that payment to the surety would constitute a voidable preference under Section 60(a) of the Bankruptcy Act, has no application here since the statute deals expressly with a transfer of the property of the debtor, and here the bankrupt had no right to the fund except to the extent that a surplus might remain after full payment to labor and material creditors (and to the surety which became subrogated to their rights) and that therefore the bankrupt had no property capable of transfer under the provisions of Section 60(a).

The two orders of the Referee (the second on a motion for reargument) were confirmed by the District Court, but the order of the District Court was reversed by the Circuit Court of Appeals solely on the ground that under New York law the surety's rights are deferred to the liens obtained upon the fund by the judgment creditor and the trustee in bankruptcy.

REASONS FOR GRANTING THE WRIT.

(1) As will be shown in the brief in support of this petition, the decision below is in conflict with the decisions of the Supreme Court and of other Circuit Courts of Appeals in construing the rights of sureties under bonds given pursuant to the Miller Act and its predecessor the Heard Act; it is in conflict with the decisions of other Circuit Courts of Appeals on similar bonds given in connection with state and municipal construction contracts in which those Courts followed the federal rule of priority although contrary to the state rule and, even assuming that New York

law applies to the rights of petitioner (a surety on a bond given pursuant to a federal statute) it is in conflict with all the decisions of the New York State Courts on similar bonds given in connection with state construction contracts in which the New York State Courts laid down a rule of priority identical with that enunciated by the federal decisions in connection with federal construction contracts, and cited those federal decisions as authority for their rulings.

(2) The decision below places the surety on a Miller Act bond in the following incongruous position: The surety's liability under that type of bond is uniform throughout the country because its liability thereunder can only be determined pursuant to federal law. The bond is given pursuant to a federal statute and 40 U. S. C. A. Section 270(b) provides that every suit instituted thereon to recover for labor and materials furnished to the contractor in the prosecution of the contract must be brought "in the United States District Court for any district in which the contract was to be performed and executed and not elsewhere, irrespective of the amount in controversy in such suit * * *." However, according to the Circuit Court's decision in this case, the surety's rights under that bond would depend on the differing rules of priority of the forty-eight states. In the instant case, the work was done in Mass. and all of the creditors to whom the surety made payment were in Mass. (R., p. 47). Yet, because the fund happens to be in New York, the Circuit Court deprives the surety of rights which it might have even on the Circuit Court's interpretation of the law, if the fund happened to be in some state where the local law as regards legal and equitable liens was otherwise; albeit, the New York courts have consistently applied the federal rule of

priority on payment bonds given in connection with state contracts. Aside from the fact that the law is not as stated by the Circuit Court, logic and reason would require that where there is uniformity of liability, there should also be uniformity of right, which is in effect only the reiteration of the rule discussed in Point I of the brief in support of this petition, that where a bond is given and executed pursuant to a federal statute, that only federal law and not local law should control the surety's rights thereunder.

(3) The case is an important one of general interest. It affects all sureties executing Miller Act bonds. The Circuit Court's decision creates doubt and confusion as to the rights of such sureties and upsets what was generally accepted as the law for many years. It overrides decisions of long standing, both of the Supreme Court and of other Circuit Courts of Appeals and tends to throw into chaos the entire field of case law on this type of bond developed throughout the past fifty years.

CONCLUSION.

In view of the foregoing, it is respectfully submitted that this petition for a writ of certiorari should be granted.

Respectfully submitted,

SAMUEL GOTTESMAN,
Attorney for Petitioner.

New York City, October, 1948.

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 FERRY BRICK COMPANY,

Respondents.

**BRIEF IN SUPPORT OF PETITION
 FOR WRIT OF CERTIORARI.**

Preliminary Statement.

The Referee's opinions which were confirmed by the District Court without opinion, appear in R., pp. 63-68. The Circuit Court's opinion appears in R., pp. 72-76. The facts, which were stipulated, appear in R., pp. 36-47.

The matters dealing with this Court's jurisdiction, the federal statute involved, the questions presented, the statement of the case and the reasons for granting the writ are all set forth in the petition *supra*, to which reference is respectfully made.

POINT I.

The rights of petitioner are governed solely by controlling federal law and not by local law.

The Circuit Court, in its opinion, held that petitioner's rights must be determined under New York law and cited Collier on Bankruptcy [14th Ed.] Section 70.62. In so doing, however, it overlooked Section 70.70 of Collier's, entitled "State Law, or Federal Law Where Applicable, Determines Existence and Effect of Liens or Other Claims", which states at page 1348:

"Of course, in the unusual case where a federal statute is invoked as the basis for a lien or claim, that statute as interpreted by the federal courts will control."

Erie Railroad Co. v. Tompkins, 304 U. S. 817, is not to the contrary. There, the late Mr. Justice Brandeis points out at page 822:

"Except in matters governed by the Federal Constitution *or by Acts of Congress*, the law to be applied in any case is the law of the states." (Emphasis supplied.)

In *Henningsen v. United States Fidelity & Guaranty Co.*, 208 U. S. 404, which involved as does here the priority rights of a surety under a Miller Act bond (then the Heard Act), Mr. Justice Brewer, in the very first sentence of his opinion points out that the grounds of suit and relief were based on statutes of the United States.

In *Prudence Realization Corp. v. Geist*, 316 U. S. 89, the late Mr. Chief Justice Stone said at page 95:

"Nothing decided in *Erie v. Tompkins supra* requires a court of bankruptcy to apply such a local rule governing the liquidation of insolvent assets. * * * In the interpretation and application of federal statutes, federal, not local law applies."

As was pointed out by petitioner in its petition for rehearing in the Circuit Court, R., p. 82, Collier's 1946 Cumulative Supplement at Page 79, Vol. 4, criticizes the 1943 decision of the Sixth Circuit in the *Matter of Zaepfel & Russell Inc.*, affirmed *sub nom.*, *Farmers State Bank v. Jones*, 135 Fed. (2d) 215, where the court, on a state contract, applied the federal rule of priority and sustained the claims of the surety company and overruled the claims of two banks to priority over the proceeds of a building contract held in the hands of a trustee in bankruptcy. Collier's reasoning is that a prior decision of the Sixth Circuit in *Farmers Bank v. Hayes*, 58 Fed. (2d) 34, which rejected the Kentucky rule of priority and applied the federal rule (on a bond given in connection with a state contract), while it may have been good law in 1932 when the *Farmers Bank* case was decided, was not good law today in the light of *Erie R. Co. v. Tompkins supra*. Collier's ends its discussion, however, with the following significant statement:

"We conclude, therefore, that the case at bar was correctly decided, only if the surety was a federal surety."

It will be seen that while Collier's criticizes the application of the federal rule of priority to a payment bond given in connection with a state contract, it ap-

proves the application of the federal rule to a federal surety. Here, the petitioner was a federal surety. Furthermore, in discussing the *Prairie State National Bank v. U. S.*, 164 U. S. 227 case, and the *Henningsen* case *supra* (which laid down the federal rule of priority which has been followed through all the years), and in referring to the statement in the *Henningsen* case that the surety's rights and obligations involve a federal matter, Collier's states:

"This is not unreasonable, since it would be desirable to have a uniform rule on the rights and liabilities of sureties to the United States."

POINT II.

New York law is the same as the federal law insofar as the surety's equitable right of priority on this type of bond is concerned.

The Circuit Court, by its decision, apparently conceded the existence of the surety's equitable right of priority under federal law, but by applying New York State decisions having nothing to do with the rights of sureties under Miller Act bonds or with the rights of sureties under similar bonds given in connection with state construction contracts, held that the surety's right in the instant case was deferred to the liens of the judgment creditor and the trustee in bankruptcy.

In so doing, however, the Circuit Court completely disregarded the fact that the New York Courts, whenever called upon to decide the rights of sureties under a similar bond in connection with a state contract, have applied the federal rule of priority.

In *Scarsdale National Bank & Trust Co. v. U. S. Fidelity & Guaranty Co.*, 264 N. Y. 159, the New York Court of Appeals had before it the conflicting claims of a surety on the performance bond of a contractor and a bank which had advanced moneys to the contractor on the strength of an assignment of the moneys due the contractor from the state, the contractor having defaulted and the surety having completed the contract at a loss. The Court of Appeals, citing *Prairie State Bank v. United States*, 164 U. S. 227; *Henningsen v. U. S. Fidelity & Guaranty Company*, 208 U. S. 404, and others, held that the equity in favor of the surety arose at the time of the giving of its bond and that the right became available when the surety completed the work at a loss and that since the equitable lien arose at the time of the execution of the bond, it was superior to the assignment.

Century Cement Mfg. Co., Inc. v. Fiore, 264 App. Div. 475, involved the conflicting claims of an assignee of the contractor and the surety on a payment bond to the balance in the hands of the state. The New York Appellate Division citing *Martin v. National Surety Company*, 300 U. S. 588, and *Scarsdale National Bank & Trust Co. v. U. S. Fidelity & Guaranty Co.*, *supra*, held the surety entitled to that balance, and stated at page 480:

"The fact that the 'completion' bond was involved in the *Scarsdale* case and the 'material and labor' bond in the instant case is immaterial

* * *

"The rule that the surety company's equitable lien arose at the time of the execution of the bond and is accordingly superior to a subsequent

assignment is established by ample authority. The principle is enunciated in *Prairie State Bank v. United States* (164 U. S. 227). It is supported by a line of Federal court decisions, including *Maryland Casualty Co. v. Board of Water Comrs.* (66 F. (2d) 730); *Lacy v. Maryland Casualty Co.* (32 id. 48); *Henningsen v. U. S. Fidelity & Guaranty Co.* (208 U. S. 404); *Hardaway v. National Surety Co.* (211 id. 552), all cited as authority in the *Scarsdale* case."

In *Municipal Housing Authority v. Hatfield Electric Corp.*, 264 App. Div. 99, the New York Appellate Division, Fourth Department, followed the same rule in a case again involving the rights of a surety under a payment bond and said at page 103:

"We are of the opinion that the surety became subrogated to the moneys in the hands of the housing authority. That right arose at the time the surety executed the bond. (*Scarsdale National Bank & Trust Co. v. U. S. F. & G. Co.*, 264 N. Y. 159). The contractor had no interest in the fund which he could pass to the bank at the time the assignment was executed and delivered. The judgment appealed from should be reversed on the law and facts and judgment entered in favor of the appellant Aetna Casualty & Surety Company."

The latest New York Court of Appeals case on this subject, decided in July 1947, is *U. S. Fidelity & Guaranty Company v. Triborough Bridge Authority*, 297 N. Y. 31, in which the Court reaffirmed its decision in *Scarsdale National Bank & Trust Co. v. U. S. F. & G. Co.*, *supra*, and cited with approval

Prairie State Bank v. United States, supra, and held that a surety which had made payment to labor and material creditors on a bond given in connection with a state contract was entitled, by virtue of its equitable lien to the fund in the hands of the Triborough Bridge Authority as against the United States Government, which had filed a tax lien for taxes owed by the contractor.

POINT III.

The decision below is in conflict with decisions of the Supreme Court and of other Circuit Courts of Appeals.

Prairie State National Bank v. U. S., 164 U. S. 227, first established the law that where a surety completes a defaulted contract of its principal, it becomes entitled to the moneys in the hands of the Government applicable to the completion of that contract, ahead of any other creditor. *Henningsen v. U. S. Fidelity & Guaranty Co.*, 208 U. S. 404, established the law that where the contractor has himself completed the contract, but has failed to pay for labor and material, the surety paying the laborers and materialmen under its payment bond is likewise subrogated to the original and continuing equitable priority in the fund, of those laborers and materialmen.

In *Belknap Hardware & Mfg. Co. v. Ohio River Contract Co.*, 271 Fed. 144 (C. C. A. 6) (1921), the Circuit Court, in discussing the *Henningsen* case, *supra*, said at page 148:

“* * * we think the necessary effect of the decision is to hold that the laborers and material-

men, in spite of or in addition to the giving of the bond, had an original and continuing equitable priority in the fund and that it was this right to which the surety was subrogated."

and at page 151:

"We therefore conclude that the labor and material claimants are entitled to priority in the distribution of the funds in the receiver's hands as against other creditors."

In *United States Fidelity & Guaranty Co. v. Sweeney*, 80 F. (2d) 235 (1935), the Eighth Circuit held that the surety was bound by contract to pay the claims for labor and material, and upon paying those claims it was entitled to be subrogated to the superior equities of the laborers and materialmen, and that when the surety made payment, its rights related back to the date of its bond.

In *Farmers Bank v. Hayes*, 58 F. (2d) 34, the Sixth Circuit rejected the Kentucky rule of priority and applied the federal rule on a bond given in connection with a state contract and held that the right of the surety to the fund there in question was settled by a long line of federal and state cases. The court there stated that whether in that particular case the surety's rights arose out of subrogation to the rights of the board of trust (under whose jurisdiction the work was performed) or the equitable liens of the laborers and materialmen, the result was the same and that in either case, the equitable rights of the surety became fixed as of the date of the bond and were "* * * superior to those of any holder of an after acquired lien".

In *Cox v. New England Equitable Insurance Company, Inc.*, 247 Fed. 955, the Eighth Circuit had before it a case on all fours with the instant case, and at that time the provisions arming the trustee with the right of a creditor holding a lien now contained in Section 70c of the Bankruptcy Act, was part of the then Section 47a(2). There the contractor on a government contract had completed the work but had failed to pay labor and material claims. The government made the final payment to the contractor, who deposited it in his bank and the bank credited the same upon the contractor's indebtedness to it. The contractor was subsequently adjudicated a bankrupt and his trustee recovered the money from the bank as an unlawful preference. There, as in the instant case, the surety claimed the fund from the trustee and the Circuit Court held that since the surety had a lien upon the fund while it was in the hands of the government, that such lien was not lost since the fund had been fully and accurately traced into the hands of the trustee. In the instant case, the existence, identity and tracing of the fund is conceded.

In *Moran v. Guardian Casualty Co.*, 76 F. (2d) 437, there was also involved a contest between a receiver and a surety on the bond of a contractor with respect to a fund paid over by the government to the receiver and which represented the balance due the contractor for work done under a government contract, the surety having made payment of labor and material claims under its bond. The Circuit Court affirmed the decision of the lower court and held that the surety had a superior lien upon the fund in the hands of the trustee in bankruptcy.

In *Philadelphia National Bank v. McKinlay, Trustee*, 72 F. (2d) 89, cert. den., 293 U. S. 583, the Court of Appeals for the District of Columbia, in a case which likewise involved a fund in the hands of a trustee in bankruptcy, held that in no case could the fund be considered due the bankrupt, and hence to its trustee, for the trustee had no greater interest than the bankrupt at the date of bankruptcy, and that at the time of the bankruptcy, the only right which the bankrupt could assert to any of the fund in question was contingent upon there being a surplus after the reimbursement of its surety, whose obligation was not only to do the work, but to pay for labor and materials.

In *re L. H. Duncan & Sons*, 127 F. (2d) 640, involved a controversy between the trustee in bankruptcy and the surety on the contractor's bond in connection with a Pennsylvania works contract. There, the Third Circuit held that the surety's right of subrogation to laborers and materialmen in the fund was paramount to the right of the trustee in bankruptcy.

In the *Matter of Zaepfel & Russell, Inc.*, affirmed *sub nom., Farmers State Bank v. Jones*, 135 Fed. (2d) 215, the Sixth Circuit, on a state contract, affirmed the decision of the District Court, 49 Fed. Supp. 709, which had in turn confirmed the order of the Referee in Bankruptcy which sustained the claims of ~~two~~ the ~~eties~~ ~~banks~~ to priority over the proceeds of a building contract held in the hands of the trustee in bankruptcy. The District Court stated clearly that the question of priority depended upon whether the court followed the rule adopted by the federal courts or

the rule announced by the Court of Appeals of Kentucky and then went on to follow the federal rule.

The decision of the Circuit Court in the instant case to the effect that the trustee's lien was superior to that of the surety is clearly in conflict with the cases above cited. Its decision that the judgment creditor's lien is superior to that of the surety is also in conflict with those cases above cited which hold that the contractor had no right to the fund and that the same did not belong to him except to the extent that any surplus might remain after reimbursement of his surety. Obviously, the judgment creditor could not acquire a lien on that which was not the property of the bankrupt. Yet, the Circuit Court in this case, by the application of New York State decisions having nothing to do with the rights of a surety under a Miller Act bond or the rights of sureties on bonds given in connection with state contracts, has arrived at the unusual conclusion that the judgment creditor of the bankrupt, by the service of its Third Party Order, acquired a lien on a fund which, by the weight of authority, never belonged to the bankrupt.

The suggestions in the Circuit Court's opinion that it was questionable whether the surety's lien extended to any other amounts other than the reserved percentage is likewise in conflict with the decisions of the Supreme Court and of other Circuit Courts of Appeals and will cause considerable havoc in the application of funds arising out of government contracts. The overwhelming weight of authority of all of the cases hereinbefore cited does not limit the surety's rights to the retained percentages only, but refers instead to the "fund" or "funds". The effect of this entire body of case law would be destroyed if the surety's lien were held to apply only to the insignificant por-

tion of the contract represented by the reserved or retained percentages. The doctrine underlying all the decisions on this subject is founded upon the principle that since a labor or material creditor cannot under the law file a lien against government property for the protection of his rights, that the moneys applicable to the performance of the government contract shall be available for his benefit and for the benefit of the surety which is subrogated to his rights.

Not only does the overwhelming weight of the federal decisions not so limit the rights of the surety, but none of the New York decisions in connection with payment bonds on state contracts so limit them. In *U. S. F. & G. Co. v. Triborough Bridge Authority*, 297 N. Y. 31 (1947), the controversy concerned the "final payment due under the contract" and not merely the retained or reserved percentages, and it was to that final payment that the New York Court of Appeals held the surety subrogated ahead of the rights of the government which had filed a tax lien for taxes owed by the contractor.

In *Lacy v. Maryland Casualty Co.*, 32 Fed. (2d) 48, the Circuit Court, citing cases including *Prairie State National Bank v. United States* and *Henningsen v. United States Fidelity & Guaranty Co.*, *supra*, clearly met the proposition here discussed and said:

"The question arises whether this superior equity of the surety extends to the current estimates payable under the contract or merely to the retained percentages. We think that it extends to both."

The extent to which the Circuit Court's decision in the instant case is in conflict at this point with the decisions of other Circuit Courts is perhaps best illustrated by the decision of the Eighth Circuit in *London & Lancashire Indemnity Company of America v. Endres*, 290 Fed. 98. In that case the bankruptcy court allowed the surety's claim, but refused to give it preference in payment out of a fund which came into the hands of the contractor's trustee in bankruptcy and which represented extra compensation, beyond the contract price, voted to the bankrupt contractor by an Act of Congress. The trustee there contended that inasmuch as the fund in his hands was not part of the original contract price, that the surety acquired no lien thereon. The Circuit Court stated that it was argued that the appropriation was a mere gratuity and having been given without legal obligation to do so, no rights could be asserted against it. The Court held however, that it was not a mere gratuity, but was further compensation for the construction work in question and in that sense should be regarded as an increase to the consideration named in the contract. The Court, citing *Henningsen v. U. S. F. & G. Co.* and *Prairie State Bank v. United States, supra*, held in favor of the surety, reversed the order below and directed preferential payment to the surety out of the appropriation to the extent of its loss.

In the *Endres* case, there was not involved any question of either retained percentage or final payment under the contract, but instead a payment voted by Congress dehors the contract. Yet, the Circuit Court held the surety entitled, to the extent of its loss, to a lien on the fund voted by Congress.

In the instant case, the Circuit Court stated that it did not feel it necessary to determine the question

of whether the surety's right of subrogation was limited only to the reserved or retained percentages, in view of its finding that the liens of the trustee in bankruptcy and of the judgment creditor were superior to those of the surety. However, the question is of such vast importance to all sureties on government contracts, and the Circuit Court's decision so far in conflict with the weight of authority, that that issue should also be passed upon by this Court in order to forestall the serious conflicts and impediments which must necessarily arise in the future by this erroneous dictum of the Circuit Court.

CONCLUSION.

In view of the foregoing, it is respectfully submitted that this Court should grant the writ of certiorari prayed for in the petition to which this brief is annexed.

Respectfully submitted,

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